

PBGC Reform: Mending the Pension Safety Net

Bill Number:

Hearing Date: April 26, 2005, 10:00 am

Location: SD430

Witness:

Alan Reuther

United Auto Workers, Washington, DC

Legislative Director

Testimony

The UAW appreciates the opportunity to testify before the Subcommittee on Retirement Security and Aging of the Senate Committee on Health, Education, Labor and Pensions on the subject of: "PBGC Reform: Mending the Pension Safety Net." We look forward to working with the Subcommittee as it considers the important issues relating to the Pension Benefit Guarantee Corporation (PBGC) and the funding of single-employer defined benefit pension plans (hereafter referred to as "pension plans").

The UAW represents 1,150,000 active and retired employees in the automobile, aerospace, agricultural implement and other industries. Most of our active and retired members are covered under negotiated pension plans.

The UAW has a long and proud history of involvement in legislation relating to these pension plans. We were in the forefront of the decade long struggle to enact ERISA, which led to the establishment of the PBGC. We also were actively involved in the enactment of legislation in 1987 and again in 1994 to strengthen the funding of pension plans and the PBGC.

The UAW believes Congress should adopt balanced proposals that will bolster the PBGC and the security of pension benefits for workers and retirees. We also support measures to strengthen the funding of pension plans and encourage employers to continue these plans.

Unfortunately, the package of proposals advanced by the Administration will not achieve these objectives. In our judgment, the Administration's pension proposals are dangerous and counterproductive. They would punish employers who are already experiencing financial difficulties, resulting in more pension plan terminations and loss of retirement benefits, more bankruptcies, plants closings and layoffs, more liabilities being dumped on the PBGC, and more employers choosing to exit the defined benefit pension system. As a result, these proposals would be bad for employers, bad for workers and retirees, bad for the PBGC and bad for the entire defined benefit pension system.

The UAW urges the Subcommittee to reject the Administration's proposals, and instead to put forward a bipartisan package of proposals that will improve the funding of pension plans and bolster the PBGC, without punishing employers, workers and retirees. We stand prepared to work with the Subcommittee to achieve these objectives.

I. Relationship to Budget Resolution

The UAW believes it is imperative that Congress consider the PBGC and pension funding issues together in a deliberative manner that will enable it to formulate policies that truly benefit workers, retirees, and employers, as well as the PBGC and the entire defined benefit pension system. Pension policy should not be dictated by the need to fill a budget hole or arbitrary deficit reduction targets.

Although increases in the PBGC premium are scored as a "savings" for budget purposes, the truth is they are a tax on employers that sponsor pension plans. We believe Congress should consider the impact of such increases on companies and the pension system generally, and not simply view this as a "cash cow" to reduce the deficit.

The UAW is particularly concerned about reports that the budget resolution conference report may require the Health, Education, Labor and Pensions Committee to produce much higher "savings" attributable to the PBGC than was originally proposed in the budget resolution passed by the Senate. This in turn could preclude the adoption of sound policies that would improve pension plan funding and reduce plan terminations, but might also reduce general revenues. In addition, it could force the adoption of extreme premium increase proposals – such as those proposed by the Administration – that would impose a 60 percent increase in the flat rate premium and enormous increases in variable rate premiums levied on employers. The UAW submits that premium increases of this magnitude will drive many employers to exit the defined benefit system, thereby undermining retirement security for millions of workers and retirees and ultimately weakening the PBGC.

For these reasons, the UAW strongly urges the HELP Committee to insist on the provisions in the Senate's budget resolution relating to the PBGC, and to oppose the counterproductive House provisions.

II. Pension Benefit Guaranty Corporation (PBGC)

It is important, at the outset, to underscore that there is no "crisis" at the PBGC. As the Administration has admitted, the PBGC has sufficient assets to pay all guaranteed benefits for many years to come (at least until 2020, and possibly longer). Thus, the reports about the PBGC's growing deficit should not create a stampede towards extreme, counterproductive proposals. Congress should approach this issue in a deliberative manner, and make sure that any remedies do not cause more harm to workers, retirees, employers and the defined benefit pension system.

There is no mystery about what has caused the PBGC to have a growing deficit. In the recent past the PBGC was projecting a significant surplus. But bankruptcies in the steel industry led to the terminations of a number of pension plans with the largest unfunded liabilities ever assumed by the PBGC. Now, bankruptcies in the airlines industry are threatening to result in plan terminations with even bigger unfunded liabilities. Thus, there is no dispute that the PBGC's deficit is directly attributable to the widespread economic difficulties and bankruptcies in the steel and airline industries.

Unfortunately, the Administration has come forward with three dangerous and counterproductive proposals to address the PBGC's projected deficit. In our judgment, these proposals would unfairly punish workers and retirees. They would also punish employers who are already experiencing economic difficulties, leading to more bankruptcies and job loss, as well as more plan terminations. Moreover, these proposals would encourage employers to exit the defined benefit system, increasing the danger of even bigger pension liabilities being transferred to the PBGC.

A). Limits on PBGC Guarantees and Pension Benefits

The UAW opposes the Administration's proposals to cut the PBGC guarantees. These include freezing the guarantees when an employer files for Chapter 11 bankruptcy, and effectively eliminating any guarantee for plant closing benefits. These changes would unfairly punish tens of thousands of workers and retirees, reducing their retirement benefits and leaving them with a sharply reduced standard of living.

It is important to emphasize that, under current law, workers and retirees often lose a portion of their benefits when a plan is terminated. Because of the five-year phase in rule and other limits, workers and retirees typically lose a portion of their benefits attributable to recent benefit improvements and certain early retirement benefits. The UAW believes that these benefit losses should not be made worse by further reductions in the scope of the PBGC guarantees.

The UAW also strongly opposes the Administration's proposals to place strict, arbitrary limits on benefits provided by pension plans that are less than 100 percent funded. These proposals would have a sharply negative impact on workers and retirees. In effect, they would reduce the adequacy of retirement benefits provided by pension plans to tens of thousands of workers and retirees. We are particularly troubled by the Administration's proposals to freeze benefit accruals, which would have an especially devastating impact on workers and their families.

The UAW is also outraged by the Administration's radical proposal to prohibit pension plans from even offering plant-closing benefits. These types of benefits have been an important means of cushioning the economic impact of plant closings as companies struggle to reorganize. By making it possible for more workers to retire with an adequate income, these benefits reduce the number of workers who have to be laid off and wind up drawing unemployment insurance and retraining benefits. It makes no sense, therefore, to prohibit plans from even offering this type of benefit, regardless of how well funded they may be.

The UAW also is concerned about the discriminatory impact of the Administration's proposals on blue-collar workers and retirees covered under so-called flat dollar plans. It is patently unfair to place restrictions on benefit improvements in flat dollar plans where the parties simply attempt to adjust benefits in accordance with the growth in wages, but to allow the benefit improvements that occur automatically in salary related plans for white collar and management personnel. In our judgment, any proposals should treat both

types of plans in an even-handed manner. In addition, it is unfair to outlaw plant closing benefits that primarily benefit blue collar workers, while still allowing golden parachutes for top management.

Contrary to the impression created by the Administration, current law does not allow employers and unions to “conspire” to increase benefits without regard to the funded status of a pension plan, and to then terminate the plan and dump these unfunded benefit promises onto the PBGC. By virtue of the five-year phase in rule, the PBGC may not fully guarantee all benefit improvements preceding a plan termination. Thus, so-called “death bed” benefit increases are not guaranteed and do not result in any increase in the PBGC’s liabilities.

The UAW does recognize that pension plans that are less than fully funded have experienced problems with the payment of lump sum distributions. In some cases, the payment of lump sums has drained assets from these plans, unnecessarily jeopardizing the continuation of the plans and the payment of benefits to other participants and beneficiaries. Thus, the UAW would support reasonable limitations on the payment of lump sums in such plans.

In addition, the plan reorganization process proposed by the UAW in Section II D 2 of this testimony would provide greater flexibility to adjust benefits and funding obligations in situations where an employer has filed for Chapter 11 bankruptcy. This would enable more employers in Chapter 11 cases to continue their pension plans, while protecting workers and retirees to the maximum extent possible. In our judgment, this flexible approach is far better than the arbitrary, one-size-fits-all benefit limits suggested by the Administration.

B). Premium Increases

The UAW opposes the Administration’s proposal to drastically increase the flat premium paid by all sponsors of single employer defined benefit pension plans from \$19 to \$30, and to index the premium for future increases in wages. We also oppose the Administration’s proposal to impose a huge increase in the variable rate premium charged to employers who sponsor plans that are less than fully funded, and to have the amount of this premium vary depending on the credit rating of a company.

First, the magnitude of these premium increases would impose significant economic burdens on many companies. This would be especially hard on companies that are already experiencing economic difficulties and on medium-sized and small businesses. It would also exacerbate the competitive disadvantage for many older manufacturing companies with large legacy costs.

Second, the change in the structure of the variable rate premium - specifically, linking it to a company’s credit rating - would have the perverse affect of punishing companies that are already in difficult economic situations. Again, this would exacerbate the competitive disadvantage facing many older manufacturing companies.

In light of these factors, the UAW believes the Administration's premium proposals would be counterproductive. At a minimum, these proposals would encourage an exodus of employers from the defined benefit pension system. This could undermine the retirement income security of millions of workers and retirees. It would also narrow the premium base for the PBGC, and thereby increase its financial difficulties. In the end, there is a real danger that the PBGC and the defined benefit pension system could enter into a death spiral, with a constantly shrinking premium base and growth in the pension liabilities being transferred to the PBGC.

C). PBGC Lien for Unpaid Contributions

The UAW opposes the Administration's proposal to give the PBGC a lien in bankruptcy proceedings for any unpaid pension contributions. This would punish troubled companies and their retirees, and lead to more liquidations, lost jobs and lost retiree health benefits. It could also result in more plan terminations and even greater pension liabilities being transferred to the PBGC.

Companies do not lightly take the step of filing for Chapter 11 bankruptcy. They do so only when they are experiencing significant economic difficulties and are unable to pay all debts when due. Chapter 11 bankruptcy, by definition, is a zero sum situation. To the extent one creditor is given a higher priority or greater claim on the company's assets, this necessarily means that the other creditors will receive less.

Thus, granting the PBGC a lien against a company's assets for any unpaid pension contributions necessarily means that other creditors - lending institutions, suppliers and other vendors, and the workers and retirees - would recover less. This would inevitably trigger a number of counterproductive, harmful consequences.

First, lenders would be more reluctant to provide the financing that is critically important to ensuring the successful reorganization of companies in Chapter 11 proceedings. Without this financing, there would be more liquidations and hence more job loss. Even worse, the negative ramifications on the lending community would extend to companies that have not yet filed for Chapter 11 bankruptcy, but who are experiencing economic difficulties and are potential candidates for Chapter 11. To protect themselves, lenders would be forced to charge higher costs to these troubled companies or even refuse financing. The end result could be more bankruptcies, and even more job loss.

Second, retirees would be particularly hard hit by any PBGC lien for unpaid pension contributions, since this would significantly reduce their ability to collect on claims for retiree health insurance benefits. In many of the Chapter 11 cases where there is an underfunded pension plan, the single biggest group of unsecured creditors are the retirees with their claim for health insurance benefits. If the PBGC is given a lien for unpaid pension contributions, the practical result would often be that there are no assets left to provide any retiree health insurance benefits. Thus, the net result of increasing the PBGC's recovery would be to punish the retirees - the very people the PBGC was

created to protect.

Third, other suppliers and vendors would also be negatively impacted by the granting of a lien to the PBGC for unpaid pension contributions. In many bankruptcies, this means that these other businesses would get a significantly reduced recovery for their claims. This could jeopardize their ability to continue in business, leading to a chain reaction of more bankruptcies and job loss.

Fourth, it is highly questionable whether the PBGC would ultimately benefit by being granted a lien for unpaid pension contributions. To the extent this proposal forces more companies to liquidate more quickly, there would be more plan terminations and even more pension liabilities transferred to the PBGC.

The PBGC already has significant leverage in bankruptcy proceedings because of the enormous claims it has for unfunded liabilities, and because of its ability to affect the timing and other aspects of plan terminations. There is simply no need to increase the PBGC's leverage, to the detriment of workers, retirees, employers, and the entire defined benefit pension system.

D). A Positive Approach to Strengthening the PBGC

Instead of the harmful, counterproductive proposals advanced by the Administration, the UAW believes that the PBGC can be strengthened through a number of approaches that would protect the interests of workers and retirees, employers and the entire defined benefit pension system.

1. Improve Pension Funding

First, the UAW believes that the overall funding of pension plans can be strengthened through the reforms described in Section III of this testimony. By taking steps now to improve the funding of pension plans, Congress can improve the security of benefits for workers and retirees, and also reduce the long-term exposure of the PBGC. These reforms can also encourage employers to continue defined benefit pension plans, while avoiding counterproductive burdens on employers who are experiencing economic difficulties.

2. Plan Reorganization Process

Second, the UAW supports the enactment of a new "plan reorganization" process for underfunded plans in situations where the employer has filed for Chapter 11 bankruptcy reorganization. We believe that this type of process could provide better flexibility in the adjustment of benefits and funding obligations, and thereby enable more companies in financial distress to continue their pension plans. This would be beneficial for the participants and beneficiaries because it would allow them to still have their pension plan and to keep some benefits that would otherwise be lost in the event of a plan termination. At the same time, this would be beneficial for the PBGC because it would require the

employer to continue making some contributions to the plan and prevent the unfunded liabilities from being transferred to the PBGC. Employers would also benefit from this plan reorganization option because it would provide greater flexibility in adjusting benefits and funding obligations, so that continuation of the pension plan becomes manageable.

To make sure that this plan reorganization process is not abused, the UAW believes it should only be available to employers that have already taken the difficult step of filing for Chapter 11 bankruptcy reorganization. Furthermore, the bankruptcy court should be empowered to approve benefit and funding modifications beyond those already permitted under current law only if they are approved by all of the stakeholders: that is, by the PBGC, the employer, and union (or, in the case of non-represented participants, an independent fiduciary appointed by the bankruptcy court). Finally, the permissible benefit modifications should be restricted to non-guaranteed benefits that would be lost anyway in the event of a plan termination. Permissible funding modifications should extend to thirty-year amortization of existing unfunded liabilities.

The UAW believes that this type of plan reorganization process could be a powerful tool for enabling struggling employers to continue their pension plans, while protecting workers and retirees to the maximum extent feasible, and also reducing the exposure of the PBGC. This process could provide the flexibility that is needed to address different economic situations that are presented in Chapter 11 cases, rather than the one-size fits all approach proposed by the Administration.

3. Cash Balance Plans

Third, the UAW believes that traditional defined benefit pension plans are better for workers and retirees than cash balance plans. At the same time, we recognize that cash balance plans are better than defined contribution plans or no pension plan at all. In recent years, the UAW has negotiated cash balance plans to cover new employees at Delphi, Visteon and other auto parts companies. This recognizes the difficult economic situations facing domestic producers in this industry.

Unfortunately, the continuing legal uncertainty concerning cash balance plans is causing some employers to shift to defined contribution plans or not to offer any pension plan at all. This was vividly demonstrated by the recent announcement by IBM that it would only provide a defined contribution plan for future employees. This trend is disturbing, both because it is bad for the future retirement income security of workers and retirees, and because it could further undermine the premium base for the PBGC.

For these reasons, the UAW supports legislation to resolve the legal uncertainties surrounding cash balance plans, by making it clear that they are not per se a violation of age discrimination laws. We also support allowing greater flexibility for cash balance plans in setting interest credits. At the same time, in situations where a traditional defined benefit plan is converted to a cash balance plan, we believe reasonable transition relief should be provided to older workers who are near retirement. This combination of

reforms would protect the legitimate retirement expectations of older workers, while at the same time allowing employers to remain in the defined benefit pension system (and continuing paying premiums to the PBGC) through the vehicle of cash balance plans.

4. Steel and Airline Pension Liabilities

Fourth, the UAW believes that the best way to deal with the steel and airline pension liabilities that have already or will soon be assumed by the PBGC is to have the federal government finance these liabilities over a thirty year period. This could be accomplished by having the federal government (or the PBGC) issue thirty-year bonds, and then have the federal government pay the interest on these bonds as it comes due. We believe this approach would cost the federal government about \$1-2 billion per year, depending on the magnitude of the airline pension liabilities that are ultimately assumed by the PBGC.

The UAW recognizes that the federal government is already running substantial budget deficits. But this infusion of federal funds to strengthen the PBGC can easily be afforded by our nation. For example, in its current budget, the Administration has proposed significant increases in the amounts that individuals can contribute to various individual retirement and savings accounts (so-called RSAs and LSAs). This involves a substantial tax expenditure that will flow overwhelmingly to upper income individuals. The Congressional Research Service has estimated that this proposal will cost the equivalent today of \$300 to \$500 billion over ten years. The UAW submits that these funds could better be used to strengthen the PBGC and protect the retirement benefits of average working families in defined benefit pension plans.

Whatever the difficulties, the fact remains that using general revenues to gradually finance the PBGC's steel and airline related pension deficit is better than all of the other options currently being considered. Specifically, it is better than punishing workers and retirees by cutting the PBGC guarantees. It is better than punishing companies that sponsor pension plans by drastically increasing their PBGC premiums. And it is better than punishing companies that are experiencing financial distress by giving the PBGC a greater claim in bankruptcy proceedings. These other options will inevitably hurt workers and retirees and employers that sponsor pension plans. They will also lead to more bankruptcies and job loss. And they will drive employers away from the defined benefit pension system, creating a death spiral for the PBGC.

The truth is the PBGC was never designed to handle widespread bankruptcies and pension plan terminations across entire industries, as we have seen in steel and are now witnessing in airlines. Indeed, the seminal case that led to the creation of the PBGC was the Studebaker situation, in which a single auto company went out of business and terminated its pension plan. Obviously, the entire auto industry did not go bankrupt or terminate its pension plans then.

When the PBGC was created by Congress, it was modeled after the Federal Deposit Insurance Corporation (FDIC), which insures bank deposits for individuals. The FDIC was designed to handle isolated bank failures, not the collapse of a broad section of the

banking industry. When the savings and loan crisis occurred in the 1980s, Congress wisely recognized that the costs associated with S & L failures should not be shifted onto the backs of individual depositors, nor onto the backs of other banking institutions. Congress recognized that those alternatives would impose unacceptable hardships on individuals and other banks, and would have a counterproductive impact on the rest of the banking system and our entire economy. As a result, Congress decided to have the federal government finance the S & L liabilities over many years, at a cost of hundreds of billions of dollars.

The same principles make sense in the case of the steel and airline pension liabilities that have or will be assumed by the PBGC. Shifting those costs onto workers and retirees or employers that sponsor pension plans would simply lead to unacceptable hardships and counterproductive economic consequences. The best approach - for workers and retirees, for employers that sponsor pension plans, for troubled companies and for our entire economy - is to spread those costs gradually and broadly across society by having the federal government finance them over thirty years.

This approach would not reward “bad actors”. The steel and airline bankruptcies and pension plan terminations were caused by many factors, including the policies (or non-policies) of the federal government relating to trade, deregulation, energy and health care, as well as the shocks flowing from the terrorist attacks on September 11th. In our judgment, it is entirely appropriate to now ask the federal government to help pay for the pension costs flowing from those policies and events.

Indeed, Congress already has endorsed this notion in a more limited context. In the Trade Act of 2002, Congress provided for a new 65 percent tax credit to pay for retiree health benefits for retirees whose pension plans have been terminated and taken over by the PBGC, and who are between the ages of 55-65. Through this provision, Congress effectively used general revenues to pay for part of the costs associated with providing retiree health benefits to this group of retirees. This provision was designed primarily as a response to the bankruptcies (and pension plan terminations) in the steel industry, which had resulted in thousands of steelworker retirees losing their health benefits. It reflected a recognition by Congress that our trade and health care policies had played a role in the steel company bankruptcies and the loss of retiree health benefits. The UAW submits that the same principles now justify using general revenues to pay for the pension costs flowing from the steel and airline bankruptcies and plan terminations.

Similarly, Congress has a long history of using general revenues to respond to disasters across our nation. This includes floods, hurricanes, droughts and many other types of catastrophes. The UAW submits that the devastation that has occurred in our steel and airlines industries is no less worthy of federal assistance.

There is no danger this type of approach will create a “moral hazard” leading to worse pension funding and more problems in the future. This is because the UAW is proposing that the infusion of general revenues to pay for the airline and steel pension liabilities be coupled with the package of reforms to strengthen the funding of other pension plans and

with the new plan reorganization process that will help troubled companies to continue their pension plans and reduce the future exposure of the PBGC.

III. Strengthening the Funding of Pension Plans

The UAW supports balanced legislation to strengthen the funding of pension plans. These reforms should be designed to ensure that benefits promised by employers to workers and retirees are adequately funded, thereby improving the security of these benefits and also reducing the PBGC's exposure for unfunded pension liabilities.

However, the UAW believes it is imperative that any new funding rules should be structured so as to provide predictable, stable funding obligations for employers and to reduce the volatility of required contributions from year to year. New funding rules should also encourage employers to contribute more than the bare minimum in good times, and avoid counter-cyclical requirements that punish employers during economic downturns.

Unfortunately, the funding proposals advanced by the Administration fail to meet these common sense objectives. The UAW strongly opposes the Administration's funding proposals because they would result in highly volatile pension funding obligations, would reduce incentives for employers to contribute more than the bare minimum, and would punish employers who are already experiencing economic difficulties.

A). Interest Rate Assumption

The UAW strongly opposes the Administration's proposal to require employers to use a so-called yield curve in establishing the interest rate assumption for pension plans. Under this proposal, the interest rate would be based on a near-spot rate (averaged over only 90 days), with a different interest rate being applied to each payment expected to be made by the plan based on the date on which that payment will be made.

This proposal has a number of fundamental problems. First, it would be extremely complicated, imposing considerable administrative burdens on plan sponsors. These burdens may discourage employers from continuing defined benefit pension plans (especially small- and mid-sized companies).

Second, contrary to the Administration's assertions, the yield curve would not provide greater "accuracy" in setting the interest rate assumption. Because there is no real market for corporate bonds of many durations, these interest rates would largely be fictitious.

Third, the yield curve would result in highly volatile funding requirements that would fluctuate widely as interest rates change over time. This increased volatility would create enormous difficulties for employers, who need stability and predictability in their funding obligations. Indeed, the increased volatility would be a powerful incentive for employers to exit the defined benefit system.

Fourth, the yield curve would impose higher funding obligations on older manufacturing companies that have larger numbers of retirees and older workers. As a result, it would exacerbate the competitive disadvantage that many of the companies currently have because of heavy legacy costs, and would punish companies that are already experiencing economic difficulties.

Instead of this dangerous and counterproductive yield curve proposal, the UAW urges the HELP Committee to make permanent the long term corporate bond interest rate assumption that was included in the temporary legislation enacted by Congress last year. In our judgment, this long term corporate bond interest rate assumption would provide an economically sound and accurate basis for valuing pension liabilities, would be administratively simple for plan sponsors to implement, would result in stable and predictable funding obligations for employers, and would avoid imposing unfair, counter-cyclical funding burdens on older manufacturing companies.

At the same time, the UAW urges the HELP Committee to allow employers to use collar-adjusted mortality tables in valuing their plan liabilities. This would enable employers to more accurately value the future benefit obligations, especially for older manufacturing companies with larger numbers of retirees and older workers.

B). Improving Plan Funding

The UAW strongly opposes the Administration's proposal to throw out the existing funding rules in their entirety, and to replace them with new funding rules based on spot valuations of assets and liabilities, with no smoothing mechanisms, and with funding targets tied to a company's credit rating. These changes would introduce an enormous element of volatility into pension funding requirements. This would make it much more difficult for companies to plan their cash flow and liability projections, and thus would provide yet another powerful incentive for employers to exit the defined benefit pension system. In addition, these changes would punish companies that are already experiencing economic difficulties and have poor credit ratings by imposing sharply higher funding obligations on these employers. The net result could be more bankruptcies, job loss and plan terminations, with even more unfunded liabilities being transferred to the PBGC.

Instead of this counterproductive approach, the UAW urges the HELP Committee to support changes in the existing deficit reduction contribution (DRC) rules that would lead to improved funding of pension plans, but also provide smoother, more predictable funding obligations for employers and less onerous, counter-cyclical burdens on employers experiencing a temporary downturn. We believe this could be accomplished through two changes: (1) modifying the trigger for the DRC so that it applies to a broader universe of plans, and also is triggered more quickly when a plan becomes less than fully funded; and (2) reducing the percentage of the funding shortfall that must be made up in any year, so there will be a smoother path towards full funding. These changes would help to ensure that more employers are required to make up funding shortfalls in their plans, and are required to begin taking this action sooner. At the same time, these changes would avoid wild swings in a company's funding obligations that can have negative,

counter-cyclical effects, especially on employers who are already experiencing economic difficulties.

The UAW also urges the HELP Committee to adopt changes to the general ERISA funding rules to shorten the amortization period for plan amendments from 30 to 15 years. This would bring this amortization period more in line with the average remaining working life of most participants. It would require more rapid funding of benefit improvements, and thereby help to improve the overall funding of pension plans.

Finally, the UAW supports modifying the definition of “current liability” to take into account lump-sum distributions reasonably projected to be taken by plan participants. This would require plans to provide adequate funding to cover anticipated lump sum distributions, and help to prevent situations where plans have been drained because of such distributions.

C). Credit Balances and Use of Excess Pension Assets

The UAW strongly opposes the Administration’s proposal to completely eliminate credit balances, which are currently created when an employer contributes more than the minimum required under existing funding rules. By eliminating credit balances entirely, the Administration’s proposal would have the perverse effect of discouraging companies from contributing more than the bare minimum during good economic times. This, in turn, could make the funded status of pension plans even worse.

Instead of this counterproductive approach, the UAW urges the HELP Committee to modify the existing rules regarding credit balances on a prospective basis, so that employers are required to value new credit balances according to the actual market performance of the extra amounts contributed by the employer. This would eliminate problems that have arisen when the actual market performance diverges from plan assumptions. But it would still preserve the important incentive that credit balances provide for employers to contribute more than the minimum required under the funding rules.

The UAW also supports increasing the deduction limit from 100 percent to 130 percent of current liability. This would allow employers to contribute more during good economic times, and to build up a bigger cushion to help during economic downturns.

In addition, the UAW supports modifying the current rules on the use of excess pension assets, so that employers are allowed to use these assets for health care expenditures for active and retired employees, not just for retirees. This would provide yet another incentive for employers to better fund their pension plans during good economic times, by providing greater assurance that companies can always benefit economically from surplus pension assets.

Conclusion

The UAW appreciates this opportunity to testify before this Subcommittee on Retirement Security and Aging to express our views on the subject of: "PBGC Reform: Mending the Pension Safety Net." We urge Congress to reject the Administration's harmful and counterproductive proposals, and instead to fashion a constructive package that will strengthen the funding of pension plans, protect workers and retirees, provide stability and predictability to employers that sponsor pension plans and encourage them to remain in the defined benefit pension system, and place the PBGC on a sound and sustainable path.

We look forward to working with Members of the Subcommittee as you consider these important pension issues. Thank you.